DEPARTMENT OF STATE REVENUE
LETTER OF FINDINGS NUMBER: 03-0012
Income Tax
For the Years 1999- 2001

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

## ISSUE

**I. Income Tax-Cost of Goods Sold**

**Authority:** IC 6-8.1-5-1(b).

The taxpayer protests the disallowance of certain expenses deducted as cost of goods sold on the federal Schedule C.

## STATEMENT OF FACTS

The taxpayer operates a used car lot as a sole proprietor. He reports his income from the used car lot on a cash basis with Schedule C of the federal 1040 form. The Indiana Department of Revenue, hereinafter referred to as the "department," performed both a sales and use tax audit on the business and a personal income tax audit of the taxpayer. The sales tax audit and assessment was based on information provided by the Indiana Bureau of Motor Vehicles. The adjustment significantly increased the taxpayer's gross sales. Therefore, the taxpayer's Indiana adjusted gross income also increased. After receipt of the audit assessments, the taxpayer determined that he had not declared all expenses on his federal Schedule C. The taxpayer made changes to his Cost of Goods Sold and filed Amended Individual Income Tax Returns for the tax period 1999-2001. Upon review, the department accepted all but two of the additions to the Cost of Goods Sold. The first disallowed car was a new 1999 GMC 1500 purchased on February 18, 1999 from an area GMC dealer. It was sold at a local auto auction on September 14, 1999. The car's odometer reading was four (4) miles at the time of purchase and 6,420 miles at the time of sale. The other disallowed automobile was a new 2000 GMC 1500 4x4 purchased from the same dealer on September 15, 1999. At the time of purchase, the car's odometer registered 25 miles. At the time of audit, this car had not been sold and had an odometer reading of 30,200 miles. The taxpayer protested the department's disallowance of the deduction of the purchase prices of these two vehicles from the taxpayer's income. A telephone hearing was held and this Letter of Findings results.

**I. Income Tax-Cost of Goods Sold**

## Discussion

The taxpayer deducted the purchase prices of the two automobiles from its gross income as the cost of goods sold. The taxpayer supports this position by indicating that it actually sold one of the cars and advertised the other car for sale. The taxpayer argues that the miles were put on the cars by demonstrating them, using them to pick up parts, running necessary business errands, and driving to auto auctions. The department disallowed the deduction contending that the automobiles were purchased for personal use rather than resale. The department supports this contention by indicating that most cars purchased for resale by the used car business were used and these cars were new when purchased. The first car was sold at auction they day before the second car was purchased. Although the taxpayer placed ads to sell the second car, it was not sold during the audit period. Finally the taxpayer put a significant number of miles on each car – 6,216 on the first car and 30,175 on the second.

As a cash basis taxpayer, the purchase price of the second car cannot be deducted from the taxpayer's receipts on Schedule C as a cost of goods sold until the taxpayer actually sells it. Since the car was not sold during the audit period, it is not necessary to make the determination of whether the car was purchased for resale or for personal use.

It is a question of fact to determine if the first car was purchased for resale or personal use. Pursuant to IC 6-8.1-5-1 (b) all tax assessments are presumed to be accurate and the taxpayer bears the burden of proving that any assessment is incorrect. The taxpayer argues that it actually sold the car and that proves that the car was purchased for resale. Considering all the facts, however, this argument is not persuasive. This car was purchased as a new car when most of the used car lot's cars were purchased as used cars. The taxpayer put close to 1,000 miles per month on the car. This is significantly more than normal use as a demonstrator and even a few trips to pick up a spare part for the dealership and attend auctions. Finally, it was sold the day before another new car was purchased. That new car was also driven in a manner indicating that it was for personal use rather than sitting on the lot as a car for resale. The taxpayer did not sustain his burden of proving that the first car was purchased for resale and its purchase price could be deducted from the taxpayer's income as a cost of goods sold.

## Finding

The taxpayer's protest is denied.

KMA/JMM/MR--042005